



UNITED STATES DISTRICT COURT  
FOR THE CENTRAL DISTRICT OF CALIFORNIA

February 2017 Grand Jury

UNITED STATES OF AMERICA,

Plaintiff,

v.

DAVID HOBART PAYNE,

Defendant.

SA CR No. 17-53

I N D I C T M E N T

[18 U.S.C. § 371: Conspiracy; 18 U.S.C. §§ 1343, 1346: Wire Fraud Involving Deprivation of Honest Services; 18 U.S.C. § 1952(a)(3): Use of an Interstate Facility in Aid of Racketeering Enterprises; 18 U.S.C. § 2: Aiding and Abetting and Causing an Act to be Done]

The Grand Jury charges:

COUNT ONE

[18 U.S.C. § 371]

A. INTRODUCTORY ALLEGATIONS

At all times relevant to this Indictment:

1. Healthsmart Pacific Inc., doing business as Pacific Hospital of Long Beach ("Pacific Hospital"), was a hospital located in Long Beach, California, specializing in surgeries, particularly spinal and orthopedic surgeries. From at least in or around 1997 to October 2013, Pacific Hospital was owned and/or operated by Michael D. Drobot ("Drobot") and/or an unindicted co-conspirator. James

1 Canedo ("Canedo") was Pacific Hospital's Chief Financial Officer  
2 ("CFO").

3 2. International Implants LLC ("I2") was a limited liability  
4 company, controlled by Drobot and headquartered in Newport Beach,  
5 California, that purchased implantable medical devices for use in  
6 spinal surgeries from original manufacturers and sold them to  
7 hospitals, particularly Pacific Hospital.

8 3. Pacific Specialty Physician Management, Inc. ("PSPM") was a  
9 corporation, owned and controlled by Drobot and others and  
10 headquartered in Newport Beach, California, that provided  
11 administrative and management services for physicians' offices.

12 4. Industrial Pharmacy Management LLC ("IPM") was a limited  
13 liability company, owned and controlled by Drobot, Michael R. Drobot  
14 ("Drobot Jr."), and others and headquartered in Newport Beach,  
15 California, that operated and managed a physician dispensing program.

16 5. California Pharmacy Management LLC ("CPM") was a limited  
17 liability company, owned and controlled by Drobot and Drobot Jr. and  
18 headquartered in Newport Beach, California, that operated and managed  
19 a physician dispensing program.

20 6. The California Workers' Compensation System ("CWCS") was a  
21 system created by California law to provide insurance covering  
22 treatment of injury or illness suffered by individuals in the course  
23 of their employment. Under the CWCS, employers were required to  
24 purchase workers' compensation insurance policies from insurance  
25 carriers to cover their employees. When an employee suffered a  
26 covered injury or illness and received medical services, the medical  
27 service provider submitted a claim for payment to the relevant  
28 insurance carrier, which then paid the claim. Claims were submitted



1 to and paid by the insurance carriers either by mail or  
2 electronically. The CWCS was governed by various California laws and  
3 regulations.

4 7. The California State Compensation Insurance Fund ("SCIF")  
5 was a non-profit insurance carrier, created by the California  
6 Legislature, that provided workers' compensation insurance to  
7 employees in California, including serving as the "insurer of last  
8 resort" under the CWCS system for employers without any other  
9 coverage.

10 8. SCIF, other workers' compensation insurance carriers, and  
11 personal injury insurers, along with other public and private plans  
12 and contracts, were "health care benefit programs" (as defined in 18  
13 U.S.C. § 24(b)), that affected commerce.

14 9. California law, including but not limited to the California  
15 Business and Professions Code, the California Insurance Code, and the  
16 California Labor Code, prohibited the offering, delivering,  
17 soliciting, or receiving of anything of value in return for referring  
18 a patient for medical services.

19 10. Defendant DAVID HOBART PAYNE ("defendant PAYNE") was an  
20 orthopedic surgeon who owned and operated Industrial Orthopedics  
21 Spine and Sports Medicine ("Industrial Orthopedics"), a medical  
22 clinic located in Santa Ana, California specializing in orthopedic  
23 spinal surgery and orthopedic sports medicine.

24 11. David H. Payne, MD, Inc. was a California professional  
25 corporation owned and operated by defendant PAYNE.

26 B. OBJECTS OF THE CONSPIRACY

27 12. Beginning on a date unknown but at least as early as in or  
28 around May 2008, and continuing through at least in or around April

2013, in Orange and Los Angeles Counties, within the Central District of California, and elsewhere, defendant PAYNE, Drobot, Drobot Jr., and Canedo, together with others known and unknown to the Grand Jury, knowingly combined, conspired, and agreed to commit the following offenses against the United States: Honest Services Mail Fraud and Wire Fraud, in violation of Title 18, United States Code, Sections 1341, 1343, and 1346; and Use of an Interstate Facility in Aid of Racketeering, in violation of Title 18, United States Code, Sections 1952(a)(1), (a)(3).

C. MANNER AND MEANS OF THE CONSPIRACY

13. The objects of the conspiracy were to be carried out, and were carried out, in the following ways, among others:

a. Drobot and other co-conspirators working with Drobot and/or at his direction offered to pay kickbacks to defendant PAYNE and other doctors, chiropractors, workers' compensation and personal injury attorneys, marketers, and others in return for referring workers' compensation patients to Pacific Hospital for spinal surgeries, other types of surgeries, magnetic resonance imaging, toxicology, durable medical equipment, and other services, to be paid through the CWCS. For spinal surgeries, typically, Drobot offered to pay a kickback of approximately \$15,000 per lumbar fusion surgery and \$10,000 per cervical fusion surgery, provided that equipment distributed through I2 was used in the surgery. If non-I2 equipment was used in the surgery, Drobot offered lesser kickback amounts.

b. Influenced by the promise of kickbacks, defendant PAYNE and other doctors, chiropractors, workers' compensation and personal injury attorneys, marketers, and others referred patients insured through the CWCS and other health care benefit programs to



1 Pacific Hospital for spinal surgeries, other types of surgeries, and  
2 other medical services and, at times, performed the surgeries. The  
3 patients were not informed that the medical professionals had been  
4 offered and received kickbacks to induce them to refer the surgeries  
5 and other medical services to Pacific Hospital. That information  
6 would have been material to those patients, to whom defendant PAYNE  
7 and other doctors owed a fiduciary duty to disclose any financial  
8 conflicts of interest.

9 c. The surgeries and other medical services were  
10 performed on the referred patients at Pacific Hospital.

11 d. Pacific Hospital and defendant PAYNE submitted claims,  
12 by mail and electronically, to SCIF and other health care benefit  
13 programs for: (1) in the case of Pacific Hospital, payment of the  
14 costs of the surgeries and other medical services; and (2) in the  
15 case of defendant PAYNE, payment of professional fees associated with  
16 surgeries he performed at Pacific Hospital.

17 e. As defendant PAYNE and the other co-conspirators knew  
18 and intended, and as was reasonably foreseeable to them, in treating  
19 patients and submitting claims for payment using the mails, wire  
20 communications, and other facilities in interstate commerce, Drobot,  
21 defendant PAYNE, and other co-conspirators concealed material  
22 information from patients, SCIF, and other health care benefit  
23 programs, including the fact that Drobot offered, paid, or caused to  
24 be paid, kickbacks to defendant PAYNE and others for the referral of  
25 surgeries and other medical services to Pacific Hospital for which  
26 Pacific Hospital and defendant PAYNE were submitting claims.

27 f. The health care benefit programs paid Pacific  
28 Hospital's and defendant PAYNE's claims, by mail and electronically.

1           g.     Drobot and others paid and caused others to pay  
2 kickbacks -- using the mails and other facilities in interstate  
3 commerce -- to defendant PAYNE and other doctors, chiropractors,  
4 marketers, and others who had referred patients to Pacific Hospital  
5 for surgeries and other medical services.

6           h.     To conceal the nature of the kickback payments from  
7 both health care benefit programs and patients, Drobot, through one  
8 of the companies he owned and/or operated, entered into bogus  
9 arrangements with the doctors, including defendant PAYNE,  
10 chiropractors, marketers, and others. The services discussed as part  
11 of those arrangements were, in fact, generally not provided; rather,  
12 the compensation was paid, entirely or in part, depending on the  
13 arrangement, to cause defendant PAYNE to do surgeries at Pacific  
14 Hospital. The bogus arrangements defendant PAYNE and Drobot entered  
15 into included, but were not limited to, a collections agreement and a  
16 physician office dispensing program management agreement.

17           i.     Drobot and others kept records of the number of  
18 surgeries and other medical services performed at Pacific Hospital  
19 due to referrals from the kickback recipients, as well as amounts  
20 paid to the kickback recipients for those referrals. Periodically,  
21 Drobot and others amended the bogus contracts with the kickback  
22 recipients to increase or decrease the amount of agreed compensation  
23 described in the contracts, in order to match the amount of kickbacks  
24 paid or promised in return for referrals. Drobot paid and caused the  
25 kickbacks to be paid through entities including IPM, I2, and Pacific  
26 Hospital.

27     D.     EFFECTS OF THE CONSPIRACY

28           14.    Had SCIF and the health care benefit programs known the



1 true facts regarding the payment of kickbacks for the referral of  
2 patients for surgeries and other medical services performed at  
3 Pacific Hospital, they would have subjected the claims to additional  
4 review, would not have paid the claims, and/or would have paid a  
5 lesser amount on the claims.

6 15. From 2005 to in or around April 2013, Pacific Hospital  
7 billed health care benefit programs at least approximately \$580  
8 million in claims for spinal surgeries and other medical services  
9 that were the result of the payment of a kickback. Defendant PAYNE  
10 performed or referred surgeries comprising at least approximately  
11 \$10,850,000 of the total billed amount, for which Drobot, through  
12 entities that he controlled, paid defendant PAYNE at least  
13 approximately \$450,000 in kickbacks.

14 E. OVERT ACTS

15 16. On or about the following dates, in furtherance of the  
16 conspiracy and to accomplish the objects of the conspiracy, defendant  
17 PAYNE and other co-conspirators known and unknown to the Grand Jury,  
18 committed various overt acts within the Central District of  
19 California, and elsewhere, including, but not limited to, the  
20 following:

21 Overt Act No. 1: On or about April 17, 2008, defendant PAYNE  
22 met with Drobot to discuss receiving kickbacks from Drobot for  
23 performing surgeries at Pacific Hospital.

24 Overt Act No. 2: On or about May 19, 2008, defendant PAYNE  
25 and Drobot Jr. discussed negotiating a deal where defendant PAYNE  
26 would receive payments in exchange for performing surgeries at  
27 Brotman Hospital.

28 Overt Act No. 3: On or about June 18, 2008, defendant PAYNE

1 performed spinal surgery on patient A.H. at Pacific Hospital.

2 Overt Act No. 4: On or about July 15, 2008, Drobot Jr. sent  
3 an email to an unindicted co-conspirator stating that Drobot agreed  
4 to pay IPM \$60,000 to reimburse IPM for payments to doctors including  
5 a \$10,000 payment that had been made by IPM to defendant PAYNE.

6 Overt Act No. 5: On or about July 17, 2008, Drobot Jr. sent  
7 an email stating that \$10,000 being reimbursed to IPM was for "stuff"  
8 defendant PAYNE did in the last four weeks.

9 Overt Act No. 6: On or about July 21, 2008, defendant PAYNE  
10 (on behalf of Industrial Orthopedics) and Drobot Sr. (on behalf of  
11 IPM) signed a Physician Office Dispensing Program Management  
12 Agreement.

13 Overt Act No. 7: On or about July 29, 2008, Drobot Jr. sent  
14 an email to Drobot stating that defendant PAYNE would be performing a  
15 spine surgery that week and would need to be paid \$8,000.

16 Overt Act No. 8: On or about July 29, 2008, defendant PAYNE  
17 performed spinal surgery on patient E.R. at Pacific Hospital, and  
18 used hardware manufactured by I2.

19 Overt Act No. 9: On or about October 1, 2008, IPM sent to  
20 Industrial Orthopedics a check for \$20,000.

21 Overt Act No. 10: On or about January 30, 2009, IPM sent  
22 Industrial Orthopedics three checks totaling \$26,000.

23 Overt Act No. 11: On or about February 19, 2009, Drobot Jr.  
24 sent an email to Drobot stating that IPM was taking losses by making  
25 payments to generate spines for Pacific Hospital.

26 Overt Act No. 12: On or about June 23, 2009, IPM sent to  
27 Industrial Orthopedics a check for \$10,000.

28 Overt Act No. 13: On or about August 20, 2009, Drobot Jr. sent



1 an email to defendant PAYNE telling him that Drobot would be using a  
2 collection agreement to pay him for surgeries performed.

3 Overt Act No. 14: On or about January 20, 2010, I2 sent to  
4 David H. Payne, MD, Inc. a check for \$14,000.

5 Overt Act No. 15: On or about June 29, 2011, I2 sent to David  
6 H. Payne, MD, Inc. a check for \$45,000.

7 Overt Act No. 16: On or about January 20, 2012, I2 sent to  
8 David H. Payne, MD, Inc. a check for \$50,000.

9 Overt Act No. 17: On or about June 5, 2012, I2 sent to David  
10 H. Payne, MD, Inc. a check for \$65,000.

11 Overt Act No. 18: On or about July 18, 2012, defendant PAYNE  
12 performed spinal surgery on patient J.L. at Pacific Hospital.

13 Overt Act No. 19: On or about July 18, 2012, defendant PAYNE  
14 performed spinal surgery on patient J.B. at Pacific Hospital.

15 Overt Act No. 20: On or about March 12, 2013, Canedo sent  
16 Drobot an email stating that defendant PAYNE was seeking to collect  
17 \$22,500 on surgeries that he performed and Drobot replied stating  
18 that defendant PAYNE would be paid for performing surgeries under a  
19 collection agreement.

20 Overt Act No. 21: On or about March 28, 2013, Pacific Hospital  
21 sent to Industrial Orthopedics a check for \$16,597.44.

## COUNT TWO

[18 U.S.C. §§ 1343, 1346]

17. Paragraphs 1 through 11 and 13 through 16 of this Indictment, including all subparagraphs, are re-alleged and incorporated by reference as if fully set forth herein.

A. THE SCHEME TO DEFRAUD

18. Beginning on a date unknown but at least as early as in or around May 2008, and continuing through at least in or around April 2013, in Orange and Los Angeles Counties, within the Central District of California, and elsewhere, defendant DAVID HOBART PAYNE ("defendant PAYNE"), together with others known and unknown to the Grand Jury, knowingly and with intent to defraud, devised, participated in, and executed a scheme to defraud: (a) patients of defendant PAYNE and other medical professionals of their intangible right of honest services in the performance of defendant PAYNE's and such other professionals' duties as treating physicians and medical providers by intentionally concealing the offer and acceptance of kickbacks paid to defendant PAYNE and other co-schemers; and (b) health care benefit programs as to material matters and to obtain money and property by means of material false and fraudulent pretenses, representations, and promises, and the concealment of material facts.

19. The fraudulent scheme operated, in substance, as set forth in paragraphs 13, 14, and 15 of this Indictment.

B. USE OF AN INTERSTATE WIRE

20. On or about June 8, 2012, within the Central District of California, and elsewhere, defendant PAYNE, for the purpose of executing the above-described scheme to defraud, transmitted and



1 caused the transmission of an item by means of wire communication in  
2 interstate commerce, namely, a wire communication through Federal  
3 Reserve Bank servers in Dallas, Texas, effectuating a transfer of  
4 \$65,000 from I2's City National Bank account ending in 3965 in  
5 California to defendant PAYNE's Wells Fargo bank account ending in  
6 1122 in California.

COUNT THREE

[18 U.S.C. § 1952(a)(3); 18 U.S.C. § 2]

21. Paragraphs 1 through 11, 13 through 16, and 20 of this Indictment, including all subparagraphs, are re-alleged and incorporated by reference as if fully set forth herein.

22. On or about June 8, 2012, in Orange and Los Angeles Counties, within the Central District of California, and elsewhere, defendant DAVID HOBART PAYNE ("defendant PAYNE") used, aided and abetted the use of, and willfully caused the use of, a facility in interstate commerce, namely, the wire communication identified in paragraph 20 of this Indictment, with the intent to otherwise promote, manage, establish, carry on, and facilitate the promotion, management, establishment, and carrying on of an unlawful activity, namely, kickbacks in violation of California Business & Professions Code Section 650, California Insurance Code Section 750, and California Labor Code Section 3215, and thereafter performed and attempted to perform an act to promote, manage, establish, and carry on, and to facilitate the promotion, management, establishment, and

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1 carrying on of such unlawful activity, in that in or about July 2012,  
2 defendant PAYNE performed spinal surgeries at Pacific Hospital in  
3 exchange for kickbacks.

4  
5 A TRUE BILL

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8 Foreperson  
9

10 SANDRA R. BROWN  
11 Acting United States Attorney

12 

13 LAWRENCE S. MIDDLETON  
14 Assistant United States Attorney  
15 Chief, Criminal Division

16 DENNISE D. WILLETT  
17 Assistant United States Attorney  
18 Chief, Santa Ana Branch Office

19 JOSEPH T. MCNALLY  
20 Assistant United States Attorney  
21 Deputy Chief, Santa Ana Branch Office

22 ASHWIN JANAKIRAM  
23 Assistant United States Attorney

24 SCOTT D. TENLEY  
25 Assistant United States Attorney  
26  
27  
28